

Message Text

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ACTION EA-14

INFO OCT-01 EUR-25 ISO-00 SPC-03 AID-20 EB-11 NSC-10

RSC-01 CIEP-02 TRSE-00 SS-20 STR-08 OMB-01 CEA-02

CIAE-00 COME-00 FRB-02 INR-10 NSAE-00 XMB-07 OPIC-12

LAB-06 SIL-01 AGR-20 PA-04 PRS-01 USIA-15 IO-14 DPW-01

DODE-00 PM-07 H-03 L-03 ACDA-19 IGA-02 DRC-01 /246 W

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FM AMEMBASSY PHNOM PENH

TO SECSTATE WASHDC 3573

INFO AMEMBASSY TOKYO

AMEMBASSY LONDON

AMEMBASSY CANBERRA

AMEMBASSY PARIS

AMEMBASSY KUALA LUMPUR

AMEMBASSY SEOUL

AMEMBASSY BANGKOK

AMEMBASSY WELLINGTON

AMEMBASSY TAIPEI

AMEMBASSY ROME

AMEMBASSY BRUSSELS

AMEMBASSY COPENHAGEN

AMEMBASSY THE HAGUE

C O N F I D E N T I A L PHNOM PENH 11746

E.O. 11652: GDS

TAGS: EFIN, EAID, CB

SUBJ: IMF MISSION TO CAMBODIA

REFS: (A) STATE 209490 (B) PHNOM PENH 10793

1. THE IMF MISSION HEADED BY CHABRIER HAS BEEN IN PHNOM PENH FOR A WEEK. THEIR PRINCIPAL PURPOSE HAS BEEN TO PREPARE FOR THE NOVEMBER 15 ESF DONORS' CONFERENCE IN PARIS. ON OCTOBER 26, THE CONFIDENTIAL

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FUND MISSION PRESENTED ITS GENERAL VIEWS AND CONCLUSIONS TO A SPECIAL MEETING OF ESF WORKING GROUP.

2. IN GENERAL THE IMF MISSION BELIEVES SITUATION SINCE THEIR LAST

VISIT IN JULY HAS DETERIORATED. THE PRICE PICTURE PARTICULARLY HAS WORSENERD WITH PRICES NOW RISING AT AN ANNUAL RATE, IN THEIR VIEW, OF 200 TO 250 PERCENT A YEAR. THE RICE PROBLEM IS ALSO MORE SERIOUS THAN THEY HAD ANTICIPATED AND THEY SEE THE NEED FOR CONTINUED LARGE IMPORTS OF RICE IN MAGNITUDE IN EXCESS OF 200,000 METRIC TONS PER YEAR. AS A CONSEQUENCE THEY ALSO SEE AN AGGRAVATED FREIGHT PAYMENT EXCHANGE PROBLEM OF ALMOST UNMANAGEABLE PROPORTIONS. THE FOREIGN EXCHANGE PROBLEM IN THEIR VIEW IS ONE OF BASIC AND DEEPENING SERIOUSNESS.

3. INFLATION.

THEIR GENERAL VIEW OF THE PRESENT SUPER-INFLATION IS THAT IT IS PRIMARILY A SUPPLY CONSTRAINED RATHER THAN A DEMAND PULL TYPE INFLATION. THE SUPPLY LIMITATIONS STEM FROM THE INTERDICTION OF DOMESTIC LINES OF COMMUNICATION, DECREASE IN DOMESTIC PRODUCTION DUE TO THE WAR OR LIMITED AVAILABILITY OF RAW MATERIALS AND A DECLINING LEVEL OF IMPORTS IN REAL TERMS. THE DOMESTIC PRODUCTION PROBLEM, PARTICULARLY IN THE INDUSTRIAL SECTOR, IS AGGRAVATED BY A GROWING SHORTAGE OF CREDIT. IN PART THIS IS BECAUSE OF INFLATION, REAL CASH BALANCES HAVE FALLEN, AND AT THE SAME TIME THE MONETARY SITUATION HAS BEEN RELATIVELY TIGHT. RECENT MONETARY EXPANSION (IN JULY AND AUGUST) DID NOT ALLEVIATE THIS SITUATION AND REFLECTED RATHER THE NEED FOR CREDIT FOR FINANCING RICE IMPORTS BY THE GOVERNMENT.

4. BUDGET

THE BUDGETARY EXPENDITURE PICTURE IS SOMEWHAT BETTER THAN THEY HAD EXPECTED ON THE BASIS OF THEIR JULY VISIT. THEY HAD ANTICIPATED BUDGET EXPENDITURE LEVELS TO BE IN EXCESS OF 50 BILLION RIELS FOR 1973 BUT NOW THINK IT MAY BE POSSIBLE TO HOLD IT TO LESS THAN THAT PERHAPS ONLY 45 BILLION. COMMENT: ON THIS SOCRE IMF MISSION MAY BE TOO OPTIMISTIC SINCE THERE WILL BE A SECOND SUPPLEMENTAL BUDGET TO COVER CERTAIN ADDITIONAL MILITARY EXPENDITURES OF WHICH WE ARE AWARE, BUT THE FUND MISSION IS NOT. END COMMENT. THE DELAY IN THE APPROVAL OF THE BUDGET EARLIER IN THE YEAR, IN THEIR VIEW, HAD THE EFFECT

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OF KEEPING BUDGETARY EXPENDITURES DOWN BELOW PLANNED LEVELS. ON THE CIVILIAN EXPENDITURE SIDE OF THE BUDGET THEY BELIEVE THE QUARTERLY CONTROL SYSTEM WHICH HAS BEEN INTRODUCED HAS BEEN EFFECTIVE IN CONTAINING CIVIL EXPENDITURES. BUT ON THE RECEIPT SIDE, PERFORMANCE HAS NOT BEEN AS GOOD AS THEY HOPED. THEY NOW EXPECT REVENUES TO BE BETWEEN 10-11 BILLION RIELS AND THE OVERALL DEFICIT (EXCLUSIVE OF COUNTERPART) AROUND 35 BILLION RIELS. THE MISSION WAS PLEASED THAT THE GOVERNMENT HAD TAKEN ACTION ON THE VARIOUS REVENUE RECOMMENDATIONS SUCH AS 400 PERCENT INCREASE IN WATER AND ELECTRICITY RATES, RISE IN THE OFFICIAL PRICE OF RICE FROM 2,500 TO 5,000 RIELS, RAISING THE CIGARETTE TAX TO 60 PERCENT, AND THE ELIMINATION OF CERTAIN SUBSIDIES.

THE MISSION WILL MAKE FURTHER RECOMMENDATIONS PARTICULARLY AS REGARDING THE NEED FOR DRASTIC CUTS IN THE REQUESTS FOR BUDGET FUNDS FROM THE CIVIZ A#FOR 1974. THEY WILL ALSO RECOMMEND FURTHER TAX MEASURES PARTICULARLY THE ELIMINATION OF VARIOUS EXEMPTIONS AND "EXONERATIONS" FROM CUSTOMS DUTIES. THE MISSION ALSO BELIEVES THE TAX STRUCTURE SHOULD BE SIMPLIFIED (CITING THE CASE OF SIX DIFFERENT POL TAXES COLLECTEDBY TWO DIFFERENT ADMIN-ISTRATIONS). CHABRIER SAID THE IMF WILL PROBABLY PROVIDE A TAX EXPERT TO ASSIST THE GKR.

OVERALL THE BUDGET PICTURE HOWEVER THIS YEAR IS SOMEWHAT BETTER THAN LAST YEAR, MAINLY DUE TO THE INCREASING COUNTERPART GENERATIONS UNDER AID PROGRAMS.

5. BALANCE OF PAYMENTS

WITH REGARD TO THE BALANCE OF PAYMENTS, THE MISSION HAS FOUND EXPORTS A BIT BELOW WHAT THEY HAD BEEN HOPING, INVISIBLES HAVE BEEN HELD WELL BELOW LAST YEAR'S LEVELS, AND IMPORTS HELD TO "VERY LOW" LEVELS UNDER THE NOUVEAU MARCHE DES CHANGES, INDEED LOWER THAN THEY HAD THOUGH POSSIBLE. THE MISSION IS OF THE VIEW, IN FACT THAT A HIGHER IMPORT LEVEL IS BOTH DESIRABLE AND NECESSARY.

OVERALL HOWEVER THE BALANCE OF PAYMENTS PICTURE IN CY 1973 IS ROUGHLY COINCIDETN WITH THEIR EARLIER PROJECTIONS, LOWER EXPORTS AND HIGH-ER PAYMENTS FOR FREIGHT OFFSETTING LOWER INVISIBLES PAYMENTS AND LOWER THAN ANTICIPATED IMPORT LEVELS. BY THE END OF THE YEAR THE GKR'S FOREIGN ASSET POSITION SHOULD HAVE IMPROVED SOMEWHAT, BUT PRINCIPALLY THIS IS DUE TO THE REVALUATION OF THEIR RESERVE ASSETS (GOLD AND SDRS) AS A RESULT OF THE DEVALUATION OF THE DOLLAR.

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6. PROGNOSIS FOR 1974

IN 1974, THE MISSION BELIEVES THINGS WILL BE MORE DIFFICULT FOR THE KHMER ECONOMY IN GENERAL AND THEIR BALANCE OF PAYMENTS IN PARTI-CULAR. NON-RICE IMPORTS THEY ESTIMATE WILL BE HIGHER AND THEY DO NOT BELIEVE THERE SHOULD BE ANY REDUCTION IN IMPORTS UNDER THE NOUVEAU MARCH DES CHANGES. THE PAYMENT OF FREIGHT ON RICE AND OTHER PL 480 COMMODITIES PRESENTS A PROBLEM OF EXCRUCIATING DIFFICULTY. THEIR ESTIMATE OF THE IMPORT LEVEL WHICH IS NEEDED UNDER THE NOUVEAU MARCHE, EXCLUSIVE OF PL 480 FREIGHT PAYMENTS, IS AT A MINIMUM \$30 MILLION AND SHOULD BE AROUND \$40 MILLION. ASSUMING PL 480 FREIGHT PAYMENTS, OF \$25-30 MILLION, THAT WOULD MEAN AN ESF OF BETWEEN \$55-60 MILLION ON THE LOW SIDE AND \$65-70 MILLION ON THE HIGH. THE MISSION BELIEVES THAT THE GKR SHOULD MAKE A SPECIAL REQUEST TO DONOR COUNTRIES TO FINANCE FREIGHT ON AGRICULTURAL COMMODITIES, BASING THIS ON HUMANITARIAN CONSIDERATIONS IN ACCORDANCE WITH THE NEED FOR BASIC FOODSTUFFS.

THE MISSION CONCLUDED, THAT DESPITE ALL THE PROBLEMS, THE EXCHANGE AND TRADE SYSTEM SHOULD CONTINUE. THE MISSION'S JUDGEMENT IS THAT ABANDONMENT OF THE NOUVEAU MARCHE DES CHANGES SYSTEM AND SUBSTITUTING EXTENSIVE EXCHANGE AND OTHER CONTROLS WOULD BE DISADVANTAGEOUS AND PROBABLY LEAD TO A DECLINE IN REAL PRODUCTION AND RESOURCES

AVAILABLE TO THE ECONOMY. THEIR VIEW IS THAT CASH AID FOR BALANCE
OF PAYMENTS SUPPORT, AND IN ADEQUATE AMOUNTS, IS THE
PRINCIPAL AID REQUIREMENT OF THE COUNTRY.
ENDERS

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